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China, Peoples Republic of

Retail Food Sector

Shanghai Retail Sector Update

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Approved by:

Scott Sindelar

U.S. Consulate General, Shanghai

Prepared by:

Ralph Bean

Report Highlights:

The retail food sector in Shanghai continues to change at a breakneck pace. This report outlines recent changes, including the recently announced merger of China's two largest food retail companies.

Includes PSD changes: No
Includes Trade Matrix: No
Unscheduled Report
Shanghai ATO [CH2], CH

There is Chaos Under the Heavens, and the Situation Is Excellent

The retail food scene in Shanghai is in a tremendous state of ferment, as the city appears determined to reinvent the way that food is bought and sold. While the overall retail environment was outlined in the Retail Food Sector Report CH2834, events have continued to move at breakneck speed. Following is a brief outline of the current state of play in retail food markets.

Putting the Hyper into Hypermarket

Although some experts feel that Shanghai is approaching saturation levels for hypermarkets, growth in this sector is likely to continue for at least another two to three years. At present, Shanghai has roughly 70 hypermarkets being operated by 10 companies, including well-known foreign chains such as Carrefour (France), Lotus (Thailand), Metro (Germany) and Auchan (France). Despite this, both domestic and foreign companies plan further forays into this sector. U.S. retailing giant Wal-Mart has announced that it will open its first Shanghai store in 2005, with up to four more to follow. Press reports claim that Wal-Mart may open another store prior to 2005, but such reports remain unconfirmed. Another newcomer to Shanghai is Sichuan-based New Hope Group, which in February announced that it will open two Nextmart hypermarkets in Shanghai this year, followed by another in 2005. New Hope Group is China's largest private company, with massive investments in agriculture, real estate and finance. Hong Kong's Park 'n Shop has also announced plans to return to Shanghai with large scale stores, after having retreated in the 1990's, when it had focused on smaller-scale operations.

Other new hypermarkets are expected from companies already present in Shanghai, including three to four from domestic supermarket giant Lianhua and five new E-Mart super centers. Carrefour, one of the most aggressive competitors in this market, has announced plans to branch out of the hypermarket business. Carrefour, which already has 36 hypermarkets in 20 cities, plans to open a chain of small discount stores in Shanghai in partnership with Lianhua. These stores will be relatively small, and stock a limited number of house-brand items at deep discounts and will also stock produce, meat and poultry, placing them in direct competition with Lianhua and Hualian's typical small-sized supermarkets. Carrefour also has plans to open a chain of supermarket-sized stores in Beijing, in partnership with the Shoulian Group (which was formed from several local supermarket chains).

Building a Bigger Beast

Competition with foreign companies remains a key concern of local officials. To this end, local officials last week announced the merger of China's two largest retail chains, Lianhua and Hualian, both based in Shanghai. Also included in the merger is local retailer Shanghai #1 Department Store Company. The intent of the merger is to build a domestic retail giant that can compete directly with multinationals like Carrefour and Wal-Mart. Taken individually, Lianhua and Hualian already possess a nationwide reach that cannot be matched by other food retailers, foreign or domestic. Combined, the two will constitute the largest domestically owned retail chain, almost three times the size of their closest domestic competitor. It will also be the only national chain with a significant presence in China's huge

number of medium and small cities. On the downside, even before the merger the sheer size of the two companies left both spread thin and facing significant management problems. It remains unclear whether the merger will help to resolve management problems or merely add another layer to them.

Convenient Excuses

The convenience store sector in Shanghai is ripe for change. The city is home to roughly half of all the convenience stores in China. Rapid growth has caused per-store revenues to fall, and many regard the Shanghai market as over-saturated. Despite this, several foreign chains have expressed or are rumored to be interested in opening stores in Shanghai. Japan's Family Mart is already planning to open a number of stores in Shanghai. While 7-11 has received permission to open stores in Shanghai, it now appears to be focusing on Beijing's less saturated markets instead. The situation has fueled rumors of possible buyouts and mergers, leading local chains to expand further in order to increase their buyout value. Liangyou, one of the largest convenience chains in Shanghai (roughly 500 stores) recently announced changes in management, turning over daily operations to its foreign minority partner. In January, Liangyou also announced that it would receive a large cash infusion from a local investment company, a step regarded by industry analysts as the prelude to the formation of a full-fledged joint venture. At the same time, the chain changed its name to Shanghai Buddies CVS Company. The Maling Aquarius Company, parent company of the Mei (or Ma) convenience store chain, was recently reported to be openly seeking foreign investment, but company officials report that they are now focused on expanding the number of stores.

Shell Game

Buyouts and limits on foreign ownership have created a complex web of ownership structures within Shanghai's retail food sector. To keep track of the players you really do need a scorecard. Following is an incomplete read out of some of the major players in the Shanghai retail market.

Lianhua	Shanghai-based food retail chain which alternates with Hualian as the largest retail chain in China. One of the few chains that reaches into small and medium-sized cities. Focused mainly on small supermarkets, but also owns the largest convenience store chain (Quik) and a growing number of hypermarkets. The chain is spread thin, though, and suffers from management problems. Lianhua is Carrefour's joint venture partner for Carrefour hypermarkets in Shanghai, and is expected to be the joint-venture partner for Carrefour's Dia discount stores when they open.
Hualian	The other Shanghai-based food retail chain competing for the number one spot. Some sources claim that a wave of new store openings put them back on top in 2002, though others still place Lianhua at number one. Hualian's merger with Lianhua, announced last week, will create the undisputed number one retail chain in China. Lianhua is also the joint venture partner for the Lawson's convenience store chain.
Nonggongshang	Another Shanghai-based food retail chain, ranked 4 th among the domestically owned retail chains. Nonggongshang is smaller with a narrower focus than Lianhua or Hualian. Nonggongshang is also the owner of one of the largest and

	most successful convenience store chains in Shanghai, Alldays.
Carrefour	In Shanghai, Carrefour is a joint venture between the French company and Lianhua. Carrefour supermarkets are the most successful in Shanghai. Carrefour now plans to open, in partnership with Lianhua, a chain of its Dia discount stores (Dia is a Spanish subsidiary of Carrefour).
Metro	German-invested joint venture. Metro has warehouse-type discount stores across China, including locations in some remarkably distant locations. Their focus, however, is more on supplying China's myriad restaurants rather than direct sales to consumers.
E-Mart	Korean joint venture. They have a limited number of stores in the area, but have been planning new stores for quite some time now.
Auchan	Another French-invested joint venture. Although the number of stores is limited, they appear to be successful.
Lotus	Owned by Thai giant C.P. Group. The number of stores is limited at present, but C.P. is said to have ambitious expansion plans. C.P. already has a major presence in China through its ownership of feed mills, oil crushing mills and poultry production and processing ventures.
RT-Mart	A Taiwanese joint venture whose parent company in Taiwan was recently purchased by France's Auchan. RT-Mart is the parent company of the C-Store convenience store chain. RT Mart's presence in China has declined in recent years.
Quik	The largest convenience store chain in China, owned by Lianhua. Although the number of stores is very large, many are co-located with Lianhua grocery stores, acting as 24 hour outlets for the larger store.
Kedi	One of the largest and most successful convenience chains in Shanghai, Kedi also benefits from its presence in the nearby cities of Wuxi and Suzhou, where competition is less intense. Kedi is owned by Shanghai Bright Dairy Co., which recently purchased Danone's dairy processing operations in Guangzhou.
Alldays	Along with Kedi and Quik, one of the largest and most successful convenience chains in Shanghai. Owned by Nonggongshang.
Liangyou	Another major convenience store chain, similar in size to Kedi and Alldays, but lacking a deep-pockets parent company. These stores evolved from the old grain and oil stores of the pre-reform era, but are modern and well-run.
Jiadeli	A smaller food retail chain, owned by a real-estate company. Jiadeli is the owner of the HomeGains supermarket chain and the 21 convenience store chain.
C-Store	RT-Mart's convenience store chain. The number of stores is small, but they are very modern. C-Store has several stores in Suzhou, where competition is less intense than in Shanghai.
Lawsons	China's first true convenience store chain, Lawson's is a Japanese joint venture with Hualian. Though the stores are well-run and the Lawson's name has a high level of consumer recognition, the chain has not expanded to match its competitors, and is rapidly becoming a minor player in Shanghai, with 78 stores (as compared to 1,000 for Quik, 680 for Kedi and 500 for Alldays and

Maling Liangyou).
Maling is a food manufacturing company with diverse interests including a famous brand of bottled water (Aquarius) and a large (250 stores) convenience store chain called Mei (or Ma). Press reports indicate the parent food company is in financial difficulty, but the convenience chain plans to continue adding stores.